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Date of lodgement: 22-Jul-2005

Title: Open Briefing®. Incitec Pivot. MD & CFO on Profit Warning

Record of interview:

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Incitec Pivot Limited today forecast a net profit after tax before significant items (NPAT) for the current year ending September 2005 of \$32 million. This is weaker than previously expected. Julian, why has performance been so poor given the recent rains?

Managing Director and CEO Julian Segal

The rule of thumb on Australia's east coast is that the winter break occurs between Anzac Day in late April and the Queen's Birthday holiday in mid June. This year we had very dry conditions in all markets before the break occurred in the third week of June, which is very late in the season. By comparison in 2004, which we considered a disappointing year, the break occurred in late May. Unfortunately, when the break came this year, rainfall was so heavy in some districts it created flooding, and regular rainfall since then has meant many farmers have been unable to get machinery onto the paddocks to plant. So in northern New South Wales and south eastern Queensland for example, some farmers are abandoning the winter crop altogether or reducing the area planted and instead looking to plant a bigger summer crop. What this means for us is that tonnes are transferred into the 2006 financial year.

It's also become apparent that the combination of very dry conditions leading up to a late break, followed by very heavy rains in many regions, negatively impacted fertiliser usage more than expected. That's because about 30 percent of the winter crop was planted "dry" prior to the rain and, given the poor weather outlook at the time, many farmers reduced their phosphorus fertiliser rates substantially. Pre-plant nitrogen application was also down by around 50 percent in most southern

areas and cropping windows shortened, reducing both the yield potential of crops and the nutrient requirement. The late break also caused a switch to less nutrient-intensive crops. For example, feed wheat and barley rather than canola were planted in some southern areas. The third issue is that to conserve cash some farmers have switched to lower-cost, lower-margin fertilisers such as straight imported ammonium phosphates instead of superior, Incitec Pivot-manufactured Granulock.

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To what extent does the fall in profit reflect a loss of market share following the formation of Elders Landmark Fertilisers (ELF) in December 2004 and to what extent have you been able to offset this impact through increased sales to independent distributors?

Managing Director and CEO Julian Segal

Analysts had already factored the ELF impact into their profit forecasts prior to today's announcement, so the adverse weather rather than ELF is driving the profit downgrade. And savings from our restructuring program will counter the impact of increased competition on earnings.

The impact of ELF on our market share is difficult to judge given seasonal conditions. However, we've made some good progress in winning new tonnes. To date we've signed up over 50 new independent fertiliser distributors, accounting for around 300,000 tonnes of fertiliser per annum. Year to date we've sold over 90,000 tonnes to these new business partners. We're also supplying around 50,000 tonnes direct to large farmers. Our preference is to partner with our network of agents and dealers, and we're only going direct where our channel partners can't competitively supply farmers.

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What action are you taking to restore profitability to the business and what are your financial targets?

Managing Director and CEO Julian Segal

We're aggressively managing the situation and, as a first step, we're well advanced on implementing a major restructuring of the business to reduce costs. Our goal is to re-establish Incitec Pivot as a scale-driven, low-cost supplier in both manufactured and traded products capable of delivering shareholder value. We won't rely on a change to more favourable seasonal conditions to return us to the required profit levels. Indeed, our plan is to align our cost and capital base to the bottom of the weather cycle so we can deliver acceptable returns in poor years and strong returns for our shareholders in good years.

In terms of financial goals for the business, our first milestone will be to generate an economic profit – or an 18 percent return on net assets (RONA) at the EBIT level. We expect 18 percent to be well in sight at the conclusion of the 2006 year.

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Given the increased level of competition in the market, will the savings from cost cutting be adequate to ensure Incitec Pivot achieves its targeted RONA if the poor seasonal conditions recur? What further action is available to you?

Managing Director and CEO Julian Segal

The cost savings by themselves won't be enough to deliver an 18 percent RONA. We'll also need to find ways to improve the efficiency of our capital base and simplify our core business processes to further reduce costs – in our supply chain in particular.

I also passionately believe we need to continue to reinforce and enhance our business culture. This culture is based on a focus on the customer, teamwork throughout the business, a commitment to safety, health and the environment, and individual accountability by encouraging each employee to run the business as if it was their own.

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James, you're leading Incitec Pivot's restructure program and you've flagged non-recurring charges of \$25 million before tax relating to the restructure. What level of savings in annual costs do you expect to achieve as a result of the restructure and when do you expect the full benefits to be realised?

Finance Director and CFO James Fazzino

The initial target is for a sustainable reduction in costs of \$25 million per annum. That equates to an improvement of around 15 percent in our fixed-cost efficiency. We expect to exit the 2006 year at an annual rate of \$25 million in savings, but due to the timing of initiatives, not all the savings will be reflected in the 2006 results.

In terms of implementation costs, our initial estimate is \$25 million before tax – around \$22 million of which will be booked in the 2005 year and \$3 million in 2006. These costs will be separately disclosed as significant items due to their size and non-recurring nature. The final cost of the restructure will be heavily dependent on a review of assets across the business that's currently in progress. We'll update the market with the final number when plans are finalised.

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In which specific areas of the business will the savings from the restructuring occur?

Finance Director and CFO James Fazzino

We've broken the restructuring program into three streams. The first is the business restructure and what we call "quick wins." It involves the implementation of a leaner organisational structure, and key changes include the merger of manufacturing and "large" logistics – and by that we mean coastal distribution centres, procurement and supply chain planning – into a new function called supply chain. This change allows the business to better optimise the overall supply chain, better address make-versus-buy decisions, and lower costs in major manufacturing/distribution hubs such as Geelong.

Another change is that we've merged "country" logistics functions – our regional service centres and Big N distribution – into the commercial function, which is now accountable for optimising the additional assets and costs incurred in enhancing customer service via the provision of localised facilities.

Turning to quick wins, they relate to targeted cost reductions throughout the business in the supply chain and in support areas like IT and insurance. Progress is pleasing. For example, we've already negotiated a \$3 million reduction in our insurance premium for 2006 without sacrificing cover levels.

Stream one is well advanced and we've mitigated implementation risk by minimising changes to front-line sales and customer service staff. Most of the changes are in back-office functions.

Stream two is resource modelling, which involves completing an economic profit analysis of the business's key assets. It includes developing a detailed bottom-up, activity-based costing model for each site. The study will identify value-adding and value-destroying activities and assets, enabling us to align our resources to value-adding activities. We'll also use the analysis to drive cost downs, stop non-value adding activities, ensure we recover the true cost of activities from customers, and exit or redeploy assets. This work is similar in scope to the recent work undertaken by Orica in North American Mining Services that successfully turned that business around, so we're using a tried and true formula.

The final stream of the restructure involves what we call business simplification. And it's this that will make our stream one restructuring sustainable. Our focus is to stop non-value adding activity, replace bureaucracy with accountability, and simplify our key processes in order to ensure we can operate with fewer people in the business. Importantly for the customer, it will make Incitec Pivot easier to do business with. We expect this stream to lay the ground-work for a broader continuous improvement program within the business.

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In the recent first half ended March, Incitec Pivot's EBIT was negatively impacted by a less favourable Australian dollar hedging position against the US dollar and by increases in phosphate rock prices as well as by competition. Can you comment on the EBIT impact of these factors in the current second half?

Finance Director and CFO James Fazzino

In 2004 we had US\$55 million of cover in place at 58 US cents to the Australian dollar and in 2005 we have US\$50 million of cover in place at 68 cents. The full-year impact of this change will be around \$17 million, with \$10 million of that in the second half.

In terms of phosphate rock, costs have increased reflecting tighter world supply, particularly from China and Togo, and that's been compounded by higher shipping costs. We estimate the full-year impact of higher rock costs will be over \$10 million, with \$6 million incurred in the second half.

Taking into account all these factors, we expect to post a full-year EBIT of approximately \$65 million.

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Given Incitec Pivot's lower than expected volumes in the current second half, can you comment on the trend in working capital since the end of March, and in particular the trend in inventory levels? What will be the impact on full-year cash flow and do you foresee any need for inventory write-downs at the end of the period?

Finance Director and CFO James Fazzino

Working capital normally peaks in the March/April period and then is quickly converted into cash as sales are made into winter cropping markets. We have a lag time of about three months in our supply chain, and this year purchased inventory for a normal season, which was consistent with the weather outlook at that time.

The poor seasonal conditions have resulted in excess inventory in the business, and at the end of June inventories were around \$110 million above the previous corresponding period, including both price and volume impact. Our supply chain planning process has allowed us to cancel planned fertiliser purchases in the forward program, which means the position will improve before year-end. However, we'll still end up with carry-over stocks going into the 2006 season. We've also been looking to find offsets in creditors, where our suppliers are sharing some of the pain of the delayed season by extending terms, and in debtors, which we continue to control tightly.

Increased working capital is ultimately reflected in interest cost, which for the full year will be up by around \$6 million compared with 2004.

We currently don't see a need for inventory write-downs as fertiliser generally has a long shelf-life. Also, selling prices currently comfortably exceed inventory cost, so we don't have a net realisable value issue at present. However, fertiliser prices have been at cyclical highs in 2005 and accordingly, inventory valuation would be impacted by a material decline in global prices.

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Given there are two months remaining in the financial year, do you foresee any potential downside risk to today's profit guidance?

Finance Director and CFO James Fazzino

The weather's always a potential risk. This season earnings visibility is even less clear than normal. And a question still remains over the extent of fertiliser sales into the top- and side-dressing markets for the winter plant and also the sugar crop. These segments could still be materially impacted by weather conditions.

A second material downside could be a negative outcome in the Elders litigation. The case, in which rebates totalling \$8 million are in dispute, was heard in the South Australian Supreme Court in April. We fully believe in our case, and judgement from the court is expected soon.

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Julian, you've indicated the restructure is targeted at ensuring Incitec Pivot retains its leading position in the fertiliser market by being Australia's lowest-cost supplier. Is Incitec Pivot's strategy solely a price-driven one?

Managing Director and CEO Julian Segal

A low-cost strategy does not translate into a low-price strategy. It's true price is a major factor for customers, and the most efficient supplier has a clear competitive advantage. Scale is vital, but we also know we must have the best business systems, especially in IT, manufacturing and logistics. We must also have the best people, well trained and individually accountable for their part in the success of the business.

Being the lowest-cost supplier is only part of the basis for success in the market. This is why all our business improvements first take into account the absolute priority of delivering customer service, which covers products, responsiveness and convenience as well as price.

One of the major improvements the current restructure will deliver is a better responsiveness to the customer by putting in place streamlined processes that, as James said, will make it easier to do business with Incitec Pivot.

Determining what the farmer needs, and what he's prepared to pay for, is part of the challenge. Present difficulties aside, we shouldn't overlook that this is a very sound business that provides an excellent basis for long-term shareholder returns.

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Thank you Julian and James.

For more information about Incitec Pivot, visit www.incitecpivot.com.au or call James Fazzino on (+61 3) 8695 4498

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